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Revisiting the economy by taking into account the different dimensions of well-being

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Revisiting the economy by taking into account the different dimensions of well-being

Abstract
In standard economic models benevolent governments are the unique actors in charge to tackle the problem of reconciling individual with social wellbeing in presence of negative externalities and insufficient provision of public goods. Some promising practices of grassroot economics suggest however that, even a minoritarian share of concerned individuals and socially responsible corporations which internalise externalities, significantly enhance the opportunities of promoting "sustainable happiness" harmonising creation of economic, social and environmental value.

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1. Introduction

In an era of shirking budget constraints synergies between the public sector and the "grassroot economics" animated by NGOs, "socially concerned" consumers and investors are fundamental to reach Lisbon Goals.
A crucial element of Lisbon Goals is that they help us to look in a three-dimensional way to the problem of human wellbeing in the third millennium. The monodimensional approach represented by the exclusive focus on the pursuit of economic growth is integrated into a wider framework which introduces in the picture social cohesion and environmental sustainability.
Along this path it is reasonable to assume that in the future it will be normal to reason in terms of an "integrated general economic equilibrium" in which the multifarious impact of entrepreneurial activities will be properly taken into account. In the standard approach firms produce material output and the question of social and environmental externalities is tackled by governmental and regulatory authorities. In the new integrated approach looming at the horizon it will we understood that entrepreneurial activities produce other kinds of output (waste, social values, etc.) by modifying the environment and the society in which they operate. The ambitious goal of the social enterprises or of the ethical and solidarity initiatives (fair trade, microfinance, ethical banking, ethical travelling, solidarity purchasing groups) is to go beyond the dichotomy of the two moments of production and distribution by creating economic value already in a socially and environmentally sustainable way. These initiatives fully acknowledge that productive activities, beyond what is considered their standard output, generates (or destroys) natural resources, human relationships, self esteem, social capital and that, in many paradoxical cases, the strive for profit maximisation may disregard the fact that destruction of the above mentioned immaterial resources may create social and environmental problems which must be costly addressed by public authorities. The problem may then be alternatively handled by anonymous beaurocracies or by grassroot organisations which take advantage from closer proximity to the problem, attract voluntary work and develop specific skills to address the social issues at stake.
This is why it is in the absolute interest of the governments and of the regional and local authorities to work together and create synergies with the network of ethical and solidarity initiatives.

In this paper we motivate this proposition by i) looking at the interaction between material and immaterial variables in the socioeconomic environment; ii) discussing the main features of the most successful ethical and solidarity initiatives and iii) outlining the potential role of government in supporting them.

The paper is divided into six sections (introduction and conclusions included). In the second section we provide a short survey of the most prominent ethical and solidarity economic initiatives currently at stake. More specifically we focus on microfinance, fair trade, responsible tourism, solidarity purchasing groups and the grassroot participated welfare initiative called “multiparty social contract”.
In the third section we highlight the importance of the role of concerned consumers and investors in supporting these initiatives. The latter, by voting with their portfolios, may increase economic convenience of corporate social responsibility, thereby transforming it from a residual element into an important factor on which competition among different producers may be played.
In the fourth section we generalise the previously described experiences by sketching a new theoretical background under the form of an “integrated general economic equilibrium” in which firms are conceived as multi-output productive units which generate material and immaterial products and affect not just creation of economic value, but also the social and environmental quality of the socioeconomic system. In this framework we point out that socially responsible firms and concerned individuals go beyond the traditional reductionism in the conception of firms and consumers in standard economic thinking since, with their action, may reconcile creation of economic, social and environmental value. In the fifth section we finally discuss the role of local, national and EU authorities in supporting ethical and solidarity initiatives. We emphasise here that some among the most prominent of them (microfinance, fair trade, ethical banking) have prospered without any government support but that such support can significantly tilt the competitive race toward socially responsible corporations with some ad hoc regulatory or fiscal measures. The final section concludes.

2. The importance of ethical and solidarity initiatives

The most relevant initiatives of ethical and participated economy on which we focus in this paper are those of microfinance, fair trade, responsible travelling, solidarity purchasing groups and some promising grassroot welfare actions such as those of the multiparty social contract.

As it is well known **microfinance**[1] institutions represent a significant advancement in banking activities due to their superior capacity of fulfilling on of the main roles of banks in the economic system, that is, matching individuals with ideas with those having financial resources to support it, even when the former cannot financially back the required loan. Traditionally, the banking system has successfully performed some fundamental roles (quality asset transformation, liquidity services,[2] pooling of savers financial resources, project selection) but it has been incapable of lending to poor uncollateralized borrowers. This is because in the standard anthropological and economic culture borrowers are looked at with suspicions and are assumed to behave like *homines oeconomici*.[3] This strand of thought explains that asymmetric information between borrowers and lenders in three crucial phases of the lending relationship (ex ante selection of projects, interim monitoring of borrower's effort and ex post verification of results) generates the three well known pathologies of *adverse selection* (higher lending rates are likely to select worse quality/higher risk borrowers), *moral hazard* (the borrower may shirk if he is not fully monitored) and *strategic default* (the borrower may declare at the end of the project that he is unable to pay even if this is not the case).

In this mainstream line of thought the collateral is the fundamental deterrent which prevents the three pathologies and, more generally, "*homo oeconomicus*" borrowers from taking actions which are against the interest of the bank.

The success of microfinance (more than 3,000 microfinance institutions around the world, a ratio of nonperforming loans over total loans below that of the standard banking system even if borrowers are mostly uncollateralized) is leading theoreticians to revise their ideas on the lender-borrower relationship.

One of the main rationales advanced to explain the success of microfinance is the mechanism of group lending with joint liability. If group members are economically responsible in case of failure of one of their mates they have the incentive to match with good borrowers (assortative matching) and to monitor them accurately during the investment period. In this way the bank can solve the

[1] The origin of modern microfinance traces back to the creation of Grameen Bank in 1983 after a pioneering activity of Muhammad Yunus who started in 1976 to experiment the effects of lending small sums to poor borrowers without asking collateral. The development of microfinance has been astounding. The Grameen Bank has now six million borrowers and the *Microcredit Summit Campaign* at end 2006 documents the existence of 3,133 microfinance programs around the world reaching approximately 113 million borrowers and, among them, 82 millions in straight poverty conditions. The most outstanding element of the performance of MFIs is their extremely low share of nonperforming loans. According to the most systematic source of aggregate data on MFIs, - the Micro Banking Bullettin (http://www.mixmbb.org/en) which created a panel of 200 MFIs from different world continents – the average MFIs loan loss rate was 1 percent in 2005. The literature provides various interpretations for this surprising performance. The most reputed among them are the role of group lending with joint liability (Ghatak, 2000; Stiglitz, 1990 and Armendariz de Aghion, 1999), which is however neither adopted by all MFIs nor by the same Grameen after its 2000 reform, and the capacity of MFI loan officers of accumulating soft information in the Berger and Udell sense (2002) which is crucial to assess creditworthiness of small businesses.

[2] For liquidity services we mean that banks match liquid liabilities with illiquid assets. This is one of the main roles of credit intermediaries which gives real investors the possibility of running their projects even when depositors want back their money. As it is easy to understand liquidity services are also at the root of banks' fragility.

[3] As Amarthya Sen clearly explains in his 1977 paper homines economici are "rational fools". This is because this standard anthropological approach followed by economists assumes that individuals are motivated only by self interest (which is obviously the most part) and not also by simphathy (passion for others) and commitment (moral duty even when it is against self interest).

asymmetric information problem relying on the capacity of local borrowers of knowing and selecting each other.

However, large part of microfinance experience does not rely on group lending and the same Grameen Bank (the leading microfinance institution funded by Junus the recent nobel price for peace) in the second and current phase of its activity is no more based on such lending practice. As a consequence, reasons for microfinance success go beyond group lending and cannot be understood if we are not ready not modify our anthropological view of the *homo oeconomicus*. What microfinance adds to our anthropological concepts is that there are immaterial factors (dignity, social capital, self esteem) which are crucial for individual wellbeing and that a borrower's delinquent behaviour would endanger. A poor marginalised individual who has a chance of inclusion through a microfinance loan and experiences an increase in dignity and self esteem does not want to loose what he has conquered on a social point of view. In addition to it, a good system of incentives to avoid loan non restitution may also abstract from group lending and joint liability and be based on progressive lending since failure to repay current instalments may prevent the possibility of receiving the next loan.

Microfinance is included within the realm of ethical and solidarity initiatives as it directly aims at providing opportunities to individuals to escape poverty. It is also a grassroot initiative since it has been historically "subsidised" by socially responsible savers who accepted a lower return on their deposits in exchange of the moral "satisfaction" of financing the poor (we may express the same concept by saying that MFIs have conquered an *ethical premium* when they collect financial resources which allows them to pay a rate below the equilibrium market one in such circumstance).

It is also important to avoid the idealisation of microfinance. The wide range of experiences around the world include many different approaches and methodologies. From those of institutions which sacrifice their profits and whose primary goal is inclusion of the poor, to those of MFIs who are standard profit maximisers and therefore charge significantly higher loan rates to their borrowers but still do microfinance.

The experience of microfinance in Europe is much less dispersed and fragmented. It is much more difficult in our context to identify targets of potential customers. The most promising fields of action seem to be those of consumption loans to liquidity constrained borrowers, of small loans for start up of small entrepreneurial activities, of loans tailored for immigrants starting activities in Europe and, finally, of student loans.

More in general, the main problem that microfinance must tackle is its capacity of enabling borrowers to scale up, that is of giving borrowers the opportunity of access to high added value entrepreneurial activities instead of trapping them permanently into low productive activities around the subsistence level.[4] Among the thousands experiences on the field some of them are successful and some other not from this point of view. We cannot however be too severe with microfinance by demanding a degree of vertical mobility for low end classes which is never observed in the reality. A reasonable performance indicator on which we may agree is that of "intergenerational mobility". At minimum we should require that microfinance must be effective in allowing borrowers children to invest in their human capital and in giving them more opportunities than it would have occurred in the counterfactual situation.

In parallel with the development of microfinance, new **socially responsible banking initiatives** have been developed in industrialised countries. The example of Banca Etica in Italy and the action of similar banks in other European countries have shown that a bank may survive and prosper by completely changing the ranking of its priorities and by putting as its first priority the creation of

[4] From this point of view it is acknowledged that microfinance loan structure based on high frequency instalments may not help to finance long term high risk innovative projects.

social and environmental value. The history of Banca Etica demonstrates that this choice may also be economically convenient. First, if the reputation of an ethical bank is sound, it is possible for her to earn an ethical premium from investors which are willing to accept a lower return on its bonds in exchange of the satisfaction for contributing to social and environmental well being. Second, Banca Etica has helped the banking system to rediscover that its main resource is customer's trust and that, paradoxically, the obsessive search of short term profits with (profit oriented) performance incentives on bank officers could endanger such resource. This is because, if the profit performance targets need to be reached at all costs, they can trigger excess risk taking or even fraudulent behaviour at the expenses of bank customers. Such imbalance in the ranking of priorities of the banking system (that experiences such as that of Banca Etica try to revert) may therefore be at the origin of bank crises and ethical banking may therefore contribute to reduce such systemic risk.

One of the most increasingly popular initiatives of grassroot economics is **fair trade**. The idea was born in the Netherlands in the second half of the twentieth century. It is symbolically relevant that it is born in the country which was one of the pioneers of the standard North-South trade.

Fair trade goal is to promote inclusion of poor farmers in global product markets, via consumption and trade, through a package of benefits which include anti-cyclical mark-ups on prices, long-term relationships, credit facilities and business angel consultancy aimed at supporting producers' capacity building (Becchetti. Costantino, 2007). [5]

FT grew significantly in the recent past (Moore, 2004; Hayes, 2004). In the last five years net sales in Europe have grown by 40 percent per year and FT products (sold not only by specialised retailers such as "world shops" but also by most supermarket chains) have conquered significant market shares (49 percent of bananas in Switzerland, around 20 percent in the UK and 3.3 percent in the US of ground coffee according to data of the FT importers' association).

At the beginning of its history fair trade has been criticised by mainstream economists on two grounds. First, the price premium paid to marginalised primary producers in the South has been seen as a distortion of the market clearing price. Such distortion is accused to give wrong market incentives to local producers and to ultimately lead to an excess supply of primary products. Second, it has been argued that the purchase of a standard product plus a donation would be more welfare enhancing than the fair trade purchase (LeClair, 2002; Maseland and De Vaal, 2002).

Further developments of the debate led to contrast the first objection in two respects. First, the transaction between marginalised producers and local intermediaries or large transnationals which is at the basis of standard trade does not occur on the basis of equal bargaining power between the two counterparts. The situation is more akin to that of monopsony or oligopsony in which the buyer has much more market power than the sellers. As it is well known, in monopsony the price paid is below that of perfect competition and therefore a case for government intervention setting a higher minimum price arises. Fair trade may therefore be conceived as a welfare enhancing minimum price initiative promoted by private importers and socially responsible consumers. Empirical evidence of the different fair trade projects confirms that the monopsony power of moneylenders in informal credit markets and of local intermediaries transporting the product to international markets exists and is strong.

Second, the same price premium creates a different product (the fair trade coffee is different from the standard coffee, exactly as the green coffee is different from the other two) and therefore fair trade may be conceived as a general purpose innovation which creates bundles of products which are original combinations of material and ethical features. Such products have their own demand and supply schedules and therefore their (intermediate) prices cannot be seen as distortions of the

[5] Evidence for such premium on prices of coffee beans and cocoa in the last 20 years is well known, available from the authors upon request and omitted here for reasons of space.

standard products traditionally sold on the market since they are exactly the source of the innovation appreciated by ethical consumers.

The second type of objection (better a standard purchase plus a charity donation) may be counterargued by exploring more in depth fair trade characteristics. Two of the main positive effects of it are; i) “local antitrust” action which, as mentioned above, breaks the monopsony power of local intermediaries and of the monopoly of local moneylender; ii) the capacity of creating contagion on profit maximising competitors of fair trade in the distribution and in the production industries.
These two relevant effects cannot be achieved by the purchase of a standard product plus a donation.
On the second point, it is worthwhile to remark that the alliance between a minority of responsible consumers and the action of socially responsible pioneers (microfinance, ethical banks, fair trade) has the merit of triggering partial imitation on behalf of profit maximising competitors thereby increasing the level of social responsibility in the overall system. [6]

Recent impact studies on fair trade have wondered whether affiliation to fair trade really generated those benefits claimed by ethical importers. Results on Kenya and Perù compare wellbeing of affiliated and non affiliated farmers (Becchetti-Costantino, 2008; Becchetti et al., 2007). They show that the price premium is consistent and that it determines superior changes in income, consumption and human development indicators for affiliated producers with respect to the control sample. Investment in human capital is demonstrated also to be significantly higher. The limits of the initiative are that lack of complementarities with macro interventions on infrastructures may prevent interested areas to start a robust development process. The accordance of micro and macro initiatives is, as usual, the most powerful driver of change.

Ethical travelling follows a principle similar to that of fair trade since it aims at rebalancing the division of value along the value chain between local workers and large international transnationals. This initiative also pays attention to the environmental sustainability of tourism. Interesting synergies between ethical travelling and fair trade have been shown to generate significant positive effects on beneficiaries. Becchetti et al. (2007) show that marginalised producers in Perù (in the Juliaca and Chulucanas areas) being part of organisations (Minka and Allpa respectively) selling to fair trade can get with the latter prices which are more than 100% higher than those paid by local intermediaries. However, since the area in which such producers operate is also included in tours of socially responsible tourism, it has been demonstrated that the latter pay up to 30 percent more of fair trade importers. Furthermore, sales to ethical tourists have been shown to increase professional self esteem even more than those to fair traders since the former appreciate and buy final products and therefore provide a direct feedback to local producers on the quality of their goods.

A recent development in socially responsible consumption is that of **solidarity purchasing groups (SPGs)** buying products directly from local producers.

[6] One of the most remarkable features of the fair trade phenomenon is the contagion of big players in the production and distribution industry (Nestlè started in October 2005 to introduce a fair trade product in its product range, Coop UK launched its own fair trade product line, Starbuck rapidly became the main seller of FT coffee in the last years). Becchetti, Di Giallonardo and Tessitore (2007) show that, in a horizontal differentiation duopoly in which firms compete on prices and ethical features of the product, partial adoption of FT practices is the optimal strategy for profit maximising incumbents after fair trader’s entry.

We may examine characteristics of the **SPG** initiatives compared with those of fair trade. The economic problems are very similar. Also in developed countries producers of agricultural primary products are locked in the lowest part of the value chain and intermediaries and final retailers get most of the value added. The idea also here is to link directly “responsible” and concerned consumers with primary producers in order to ensure fair prices to the latter.
The SPG initiatives have also three additional advantages with respect to fair trade: discounted prices with respect with respect to standard market competitors; proximity between consumers and primary producers and a more direct and visible environmental impact. For these reasons the SPG initiative has an enormous potential and appears as economically convenient also for non concerned consumers. The desire to have genuine, lower price, local products whose production can be verified personally satisfies the taste for unsophisticated, ecological and healthy products also for consumers without particular ethical concerns.

The economics of ethical and solidarity initiatives is continuously producing new ideas and projects which provide new grassroot welfare solutions. One of the most interesting of them is the **multiparty social contract** (MSC), an initiative which enhances synergies between different grassroot actors and local institutions.
The MSC, developed experimentally in Alsace with the support of the Council of Europe, addresses the problem of individuals who fall into the plague of overindebtedness and usury. In order to solve this complex problem it creates a net of protection and solidarity involving different organisations which jointly address the social problem. The network is composed by fair trade, solidarity purchasing groups, organisations of psychotherapists, ethical banks and charity organisations. The joint action of them allows to organise an integrated action which deals with all economic and psychological aspects of overindebtedness. Side products of this initiative are the enhanced capacity of member organisations to operate together.
The success of the program consists in the transformation of the beneficiaries from part of the problem to part of the solution of it. At the end of the process they often become activists of the same multiparty social contract and try to convince other people in need to take part to it.
Consistently with the overall theoretical picture to which this paper is inspired, the success of the multiparty social contract depends on its capacity of addressing jointly all economic and psychological aspects of the overindebtedness problem. The vision behind it fully acknowledges that the life satisfaction does not depend only on material wellbeing but also by those immaterial factors such as dignity, self-esteem and trust which are fundamental drivers of the capacity of each individual to give a contribution to the society in which he lives.

3. The role of citizens

The Eisenberg principle of indeterminacy which prevents theoretical models to maintain stable features across time, due to changes in the interaction of the same factors and systems under observation, can be applied all the more so to social sciences where the “basic object” of investigation is the human being who interacts with social, economic and political variables and modifies his behaviour across time.
The indeterminacy principle applies even more to the question of the survival and growth of ethically responsible enterprises. Their success crucially depends in fact not just on internal factors such as employees motivation but also from the support of socially responsible consumers. Even in the most optimistic scenarios in which such enterprises can compete in price and quality with standard firms, the acknowledgement of an ethical premium by the public may dramatically increase their chances of success.
In this respect recent empirical advances and results from lab experiments reject the reductionist hypothesis of individuals only moved by self interest and fully support Sen’s idea that sympathy and commitment are important elements in the picture. More specifically, experiments on trust,

dictator and public good games fully reveal that, even though self interest obviously remains a dominant factor, players are also moved by inequity aversion, strategic or pure altruism and "warm glow" preferences (i.e. they get satisfaction from the pure pleasure of giving).[7]
These additional motivations of human action help us to understand why the willingness to pay for socially and environmentally responsible features of products is growing significantly. Several consumer surveys run in different OECD countries show that the share of those who would prefer a socially responsible product for the same level of price and quality is above 50 percent. The driver of this desire is not just altruism: enlightened (or longsighted) self interest may be enough. In the environmental field the link between the public and private good elements of the issue is absolutely evident. Care for environmental sustainability is not only good per se but also for the positive consequences it directly brings to any individual. This is particularly clear in two directions. First, the deterioration of a non reproducible and non appropriable resource such as climate is clearly perceived as affecting every individual even though the consequences are not the same for everyone and the poor are always less capable than the rich to protect themselves from environmental calamities.
Second, green products are extremely appreciated by consumers since the latter clearly perceive that tracking the productive chain will reduce the uncertainty about the origin and productive process of the product and the health problems which may arise from it.
Even though the link between private and public good elements for fair trade or socially responsible products is slightly more difficult to perceive, such link remains robust and should be more effectively explained to consumers. As it is well known from the economic literature, the main source of (illegal) migration is the difference in per capita income between country of origin and country of destination. Moreover, in globalised labour markets poor standard of living of unskilled workers in less developed countries is the main source of wage competition which endangers work rights of equally low skilled employees in industrialised countries.
Once these links are properly acknowledged it should be absolutely clear that socially responsible consumption and saving is a "natural" economic action which reconcile the dichotomy between our worker and consumer selves. As consumers our welfare depends directly from the difference between our maximum willingness to pay and the market price and therefore lower prices increase it. However, too low prices may create pressure on workers rights of that specific industry, but also contribute to a more general climate of pressure on workers wellbeing and therefore be in contrast with our interest as workers.
To sum up, the "portfolio vote" attributed via socially responsible consumption and investment is primarily an increase in participation and economic democracy. We vote once every four-five years for coalitions with articulated political programs of which we appreciate some, but inevitably not all, aspects. With socially responsible consumption we can vote everyday and more precisely by evaluating, not just price and quality, but also the social and environmental production of a given corporation.
A final intriguing element of this new phenomenon of grassroot action is that it contributes to increase market dignity. As it is well known the market has some important qualities - i) capacity of generating spontaneously a decentralised price clearing equilibrium which reconciles interests of a large number of anonymous consumers and producers; ii) capacity of providing right signals with prices about relative scarcity and tastes for a given products; ii) quality of being a mechanism which, from the starting point of transactors endowments, can generate a deal which is advantageous for both. What the market cannot do (or could not do so far) was a social intervention aimed at affecting the starting conditions of individuals. To make a cruel example, an extremely

[7] We refer for example to the experimental results on Ultimatum games (Camerer and Thaler 1995), Dictator Games (Andreoni and Miller 2002), Gift Exchange Games (Fehr, Kirchsteiger and Reidl, 1993, Fehr, Kirchler, Weichbold and Gächter 1998), Trust Games (Berg, Dickhaut and McCabe 1995) and Public Good Games (Fischbacher, Gächter and Fehr 2001; Fehr and Gächter 2000).

deprived individual in need of financial resources may decide to sell voluntarily his kidneys to a rich consumer. The market allows both of them to realise the transactions but cannot do anything to solve the social problem which is at the origin of such transaction.

The novelty of socially responsible consumption is that, for the first time, it is possible to use the market mechanism to address directly social issues. By financing microfinance or buying fair trade products we can at the same time vote and contribute to the inclusion of the poor and improvement of their economic conditions with a simple market action.

What is absolutely obvious and cannot be neglected is that illustrating the potential of ethical and solidarity initiatives does not imply arguing at the same time that institutions and rules are no more important, just because we discovered market mechanisms which may be used to address social issues. Such mechanisms only want to emphasize that, given the characteristics of the current economic system, there are new synergies between grassroot and institutional action which may be exploited to reinforce effectiveness of actions aimed at improving society wellbeing.

4. Toward a model of "integrated general economic equilibrium"

In this section we want to generalise the characteristics of the interaction between "ethical pioneers" and socially responsible consumers. We try to make them clearer with a small example accessible also to nontechnical readers what we mean by "multiproduct" firms and what can be the advantage of having firms who reconcile creation of economic value with social and environmental sustainability.

The standard textbook approach conceives a firm production function in the following way:

$$Y=f(K,L,H) \qquad (1)$$

The firm produces the material output Y (goods or services sold on the market) with the production function f(.) by using as inputs physical capital (K), workers (L) and human capital (H), that is, workers' knowledge accumulated through schooling years and learning on the job.

This approach completely neglects that corporate activity is more than just producing material output. What we mean here is that "immaterial" variables such as "relational goods",[8] workers self esteem,[9] interpersonal trust, social capital[10] are not the same before and after productive activity. In

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[8] According to a recent literature (Ulhaner, 1989; Gui, 2000; Gui and Sugden, 2005) relational goods are *a specific kind of local public goods which are simultaneously consumed when produced*. Examples of relational goods are, on small scale, love or family relationships and, on large scale, many kinds of social events (club or association meetings, live sport events, etc.). Relational goods are *local public goods* since nonexcludabilty and non rivalry are limited to participants. They are simultaneously consumed and produced since participating to them is both an act of production (my presence contributes to the increase in the value of the good) and consumption (I enjoy it while producing it).

They also are a special kind of public goods since they should be better defined as anti-rival than non rival. This is because their very same nature is based on the interpersonal sharing of them. As a consequence, participation to their production and consumption actually creates a positive externality on partners and contributes to the quality of the public good itself. For the same reasons partners do not see nonrivalry and nonexcludability as negative elements which prevent them from exploiting all private benefits of the good, but as positive elements which implement its value (my satisfaction is actually increased, or even crucially determined, by the fact that the other is also participating and taking pleasure).

[9] Even though the literature on self-esteem is much less extended, the debate between economists and psychologists on the causality nexus between self esteem and life events has taken a very

the same way corporate production significantly modifies the environment by producing waste, consuming resources and producing emissions.
An integrated approach to corporate activity should therefore take into account all these correlated effects and conceive the production function as follows

$$h(Y,SE,EN,MO,REL,SC)=f(L(Mo,Se,Rel),K,H,SC) \qquad (2)$$

where, on the left hand side, it is acknowledged that firms produce, in addition to material output (Y), self esteem (SE), relational goods (REL), social capital (SC), workers morale (MO) and several by-products which have strong environmental consequences. An important difference arises also on the left hand side where it is acknowledged that "immaterial factors" such as self esteem, morale and relational goods are fundamental components of workers productivity. To make just some examples on this point consider that modern corporations may be conceived as "trust game corporations" where productive output depends crucially on teamworking and on a series of complex tasks which require joint application of workers with specific nonoverlapping skills (a lawyer, an economist, an engineer, etc.) (Becchetti-Pace, 2007). The most important feature of joint work is the creation of superadditivity (a result which is more than the sum of the individual contributions of its participants). Superaddivity has two fundamental rationales. First, by explaining things to others we learn better what we think to know. Second, only by joining different pieces of the puzzle represented by individual specific know-how, we may reconstruct the overall picture and increase our knowledge in a given field.
In this framework low quality of relational goods among co-workers may seriously harm such process. The basic ingredient of it is in fact, as in the standard game theoretic literature of trust games, the decision to share information with teammates, a decision which implies the risk of abuse and exploitation of such information. In working environments in which quality of relationships among workers is lower, there will be less information sharing and no superadditivity with negative effects on corporate productivity.

In this integrated general equilibrium model individuals maximise their utility/happiness functions

$$\text{Max } U(C,MO,REL,SE) \qquad (3)$$

whose arguments are not just consumption but also the same immaterial variables (morale, self esteem, relational goods) which are both determinant of their productivity and affected by their corporate life.

The maximisation is subject to the standard constraint (4) which equals (after tax) disposable income (1-t)Y[11] to consumption (px) and savings (S). Finally, relation (5) simply acknowledges that investment equal savings in equilibrium

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similar direction with respect to that of life satisfaction. According to Tafarodi and Swann (2001) self-esteem is "the intrinsic perception of one's self in relation with other people" and is strictly related to self-confidence, representing the perceived ability of accomplishing one's own goals in life, since "…those who are liked enjoy a clear advantage in achieving their goals".

[10] Social capital generally identifies the degree of cohesion of a given community under several aspects. The most important of them are trust on institutions, interpersonal trust (under the form of trust and turstoworthiness) and willingness to pay for public goods. For the role of social capital in economic systems see Putnam (1993), Zak and Knack (2001) and for its effects on economic growth see Knack and Kiefer (1997).

[11] t stands for the income tax rate.

s.t. (1-t)Y=px+S (4)

S=I (5)

With respect to standard homo oeconomicus behaviour our approach rejects the reductionism in the conception of individual happiness function (consumption is not the only driver of life satisfaction !) but, at the same time, accepts a principle of rationality (individual behaviour responds to a strategy which maximises individual goals given time and budget constraints) which we consider a reasonable approximation of what on average happens in the reality.
Note that some of the factors determining individual life satisfaction are not subject to the budget constraint and may be increased at no cost. The question here is that their satisfaction does not depend only on the individual but by the social environment in which he lives, by the corporate climate and by the individuals with which he has relationships. To put it simply, the main constraint here is not money but *others*, that is, the disposition of partners in the production and consumption of the relational good to invest in it together with the individual at stake.

Finally, as in standard economic models we acknowledge that physical capital, a fundamental input in productive activity, follows the standard law of motion

$\dot{K}$ =I-dK (6)

In which the instantaneous rate of change of capital stock $\dot{K}$ is determined by investment (I) minus depreciation (calculated by applying the rate d to the stock of capital investment).
In this rudimentary model we also have a standard budget constraint (in which we assume for simplicity that the budget clears every period with no generation of debt).

tY=G(EN,SC,REL,SE) (7)

On the right hand side of (7) we have tax inflow and, on the right hand side, government expenditure. What we want to emphasize here is that such expenditure is a positive function of the negative social and environmental externalities (all arguments in parenthesis) created by corporations into their activities. More specifically, the volume of government expenditure is a positive function of environmental and social problems.

Imagine now to have two types of firms. The first one is the standard type of profit maximising entity which does not care about social and environmental externalities. Such firm produces material output and contributes to economic growth but, at the same time, may generate negative social and environmental externalities. On the first point (negative social externalities) we may assume that negative corporate climates may reduce quality of relational life of their workers, their morale and self esteem. Layoffs may produce marginalisation which needs to be tackled by government policies aimed at unemployed rehabilitation etc. Obviously things can go the other way round but what we want to underline here is that, in order to evaluate companies contribution to creation of economic value at aggregate level, we must consider not just the direct productive effects but als the indirect effect on the social and environmental dimension of their activities, consistently with the concept of their multiproduct production function.
With this respect the role of social enterprises can be very important here. Firms with different rankings of priorities which consider their main goal environmental sustainability and creation of social value, compatibly with their capacity of creating economic value, may maximise their positive social and environmental contribution by alleviating instead or worsening government budget. Practical examples of this are those mentioned in the previous sections and, among them,

microfinance or ethical banks which contribute to the solution of social problems with their lending schemes to *unbankables*[12] or energy saving companies who restructure houses in order to improve their environmental efficiency and therefore create economic value by reducing environmental degradation.
Several crucial questions arise here. Can socially responsible firms survive in the competitive race with the first type of firms (standard profit maximising companies)? How citizens and institutions may contribute to the picture ?
The clear synthetic suggestions which comes from the model tells us that these firms survive in that i) they compensate superior costs (required by the fulfilment of more severe social and environmental standards) with potential benefits (higher workers productivity due to the high levels of immaterial factors such as morale, self esteem and relational goods); ii) a minority of socially and environmentally concerned citizens vote with their portfolio in favour of these companies; iii) institutions support them with both non costly (regulation) and costly (tax allowances, etc.) intervention.
In the section which follows we will enter further into the details of this picture by analysing the role of institutions in the proposed framework.

5. The role of the government

Ethical and socially responsible economic initiatives have born and grown without any direct government support, even though the latter could have been of great help to them. To provide just an example fair trade would have in principle greatly benefited from a reduction of tariffs on "colonial producs" and an elimination of escalating barriers which fix higher duties on transformed products with respect to raw materials. Such initiatives would have greatly helped fair traders to increase the part of value added appropriated by marginalised producers in the South.
With regard to microfinance, as it is well known, profitability and outreach are inversely correlated and those MFI initiatives more directly targeted to the poor required subsidies to survive. However such subsidies came from foundations, socially responsible investors (accepting lower returns on their deposits to finance MFIs) and private donors and, generally, not from government.
The above mentioned features and the history of these initiatives demonstrated that their businesses are sustainable and pushed profit maximising players to enter in these fields (coops, Starbucks, Nestlè and even McDonalds and Wal-Mart recently in fair trade, and many financial institutions in microfinance).
In spite of it, at the present state of affairs, the role of the state could be of great importance to foster these initiatives and contribute to the edification of an economic system in which creation of economic value may be reconciled with social and environmental sustainability.
We must not forget that competition does not occur in a rule-free environment. On the contrary, success of one or another player does not depend only on its intrinsic quality but also on the rules of the game. This is absolutely evident in environmental regulation where new pro-environment rules (such as limited access or access charge to big metropolitan areas based on environmental quality of cars) or simply expectations of their implementation may be crucial to tilt the competitive race in favour of the more environmental-friendly producers.

More in detail, we believe that, if the government cares about redressing economic activity in a more socially and environmentally sustainable direction, and if it understands that failure to do so would imply high welfare costs, it should take two types of cost-free and costly initiatives.
The cost-free initiatives involve regulation on social rating and pro-socially responsible players procurement rules. The costly initiative concern various forms of tax allowances, once the

[12] We generally define *unbankables* all those potential borrowers lacking of a collateral and generally being refused for that by ordinary banks.

contribution of social responsibility to societal wellbeing and its positive effect on government budget is properly taken into account.
On the first point it must be considered that consumers' and investors' willingness to pay for socially and environmentally responsible features of products is extremely high according to surveys run in different parts of the worlds. As already mentioned in section 3 more than 50 percent of the population would prefer the more socially and environmentally responsible product if price and quality are the same with respect to a standard product. Around 20 percent of the population would be willing to pay up to 10 percent more for the former.
These large numbers do not often become market shares because they are based on a "virtual" choice (availability on each shelf of the above mentioned two products and full information on their characteristics) which is not available in the reality. A compulsory norm on the disclosure of social rating on companies selling products would greatly help. Such norm would not create any distortion or discrimination at country or industry level, since it would pose the same obligation on all producers selling in a given country. Furthermore, it would contribute significantly to an increase in information and in the capacity of portfolio vote of consumers and investors who would remain free to use or not the new information. As it occurs in the industry of financial rating (with S&P, Moody and Fitch), competition among the most important players should ensure that social rating information come from a variety of independent sources (in our case they may be the well established KLD, Ethibel, Eiris, etc. already selling their services to ethical investment funds and the general public).
Social rating would met into some problems which are very close to those of financial rating. Conflicts of interests between rating agencies and corporate customers (which would have to pay for the rating) could be reduced by the creation of a multistakeholder authority. Fixed costs of social rating should be an unsustainable burden for small firms and a different treatment for them should be allowed. In spite of all the inevitable limits and problems, the compulsory social rating system (on product labels or on market shelves ?) would greatly contribute to spur the debate on the issue and provide firms with the right market incentives to adopt socially responsible strategies.
The second field of (cost-free?) intervention is procurement rules. It is true that, by giving points to socially and environmentally responsible features of competitors, the public sector could be ultimately led to purchase goods and services at slightly higher prices. On the other hand, a blind application of the minimum price rule would seem nonsensical given the overall public (and Lisbon) goal of matching creation of economic value with social cohesion and environmental sustainability.

6. Conclusions

No one denies that macroeconomics, institutional reforms and infrastructures are fundamental to promote economic development and social cohesion. In the traditional western democracies grassroot voice on this issue was mainly limited to the participation to political life and, for most people participation is limited to the electoral vote.
However, global integration of market economies, the weakness of international institutions which are not directly elected and the lack of global governance rules aimed to address the issues of global public goods made always more clear that an economic system may not works by just waiting for such "top down" intervention.
In addition to it, a longstanding tradition of participated action of non governmental organisations has often demonstrated that local community organisations, which are closer to social problems and are composed by motivated members, may tackle more effectively social and environmental problems. Such organisations have proven that they can do better than the *molochs* of traditional welfare systems which often deals anonymously with beneficiaries providing scarce contribution to

the many times mentioned immaterial factors (trust, self esteem, dignity) which we showed to be so important in promoting social inclusion.
These are the reasons why quality and effectiveness of intervention in social and environmental issues will crucially depend in the future also from bottom-up participation and from the synergies between this participated action of the civil society and local, national governments and regulatory authorities.
In this paper we presented the ethical and solidarity initiatives that, at the moment, have developed and emerged as successful and sustainable models of creation of economic, social and environmental value. In presenting them we are fully aware of their limits as well as their great potential. Microfinance, fair trade, solidarity purchasing groups, ethical tourism are only examples of a more general principle which will inspire new historical realisations which we still do not see at the horizon today.
The principle is that the ultimate masters of the present economic system are neither the governments nor large corporations. Both of them crucially depend on the vote of citizens, consumers and investors. This implies that we cannot complain when we see something which we do not like since the ultimate responsibility for it is on us and on our portfolio vote.
To understand why the potential of these initiatives (which are there to remind us about our power) is enormous we may imagine what could happen if, say, 60 percent of individual would decide to give more money for solidarity or if they alternatively decide to choose products on the basis of price, quality but also social and environmental responsibility of producers. In the second case the additional advantage would be an incredible incentive for all corporations to modify their productive systems in direction of a “three-dimensional” integrated target of society wellbeing with increased consistence between creation of economic value and pursuit of social goals.
The existence of a potential does not mean that we are already there, nor it is a guarantee that we will definitely be there one day in the future.
It only reminds us of an incredible opportunity we have to solve global imbalances with simple everyday life choices.
We generally complain about the changes we would like to see in politics and economics without being aware that we may be the main actors of that change.

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